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C O N F I D E N T I A L SECTION 01 OF 02 AMMAN 007296

SIPDIS

TREASURY FOR OASIA - A. DEMOPULOS

E.O. 12958: DECL: 11/5/08
TAGS: EFIN EAID PREL JO
SUBJECT: JORDAN: IMF MISSION REVIEWS OUTLOOK

REF: A. AMMAN 6962

¶B. AMMAN 6313

Classified By: Ambassador Edward W. Gnehm. Reasons 1.5 (b) and (d).

¶1. (C) Summary. An IMF team visiting Amman sees no economic need for additional cash assistance to Jordan before December 31, given that the country's finances are currently in good shape -- although there is potential crunch next year as the level of foreign grants falls and oil import costs rise. Sharing concerns about the new government's ability to enforce fiscal restraint, the Fund staff recommended that the U.S. continue to put effective policy conditions on its cash assistance. For the longer term, the staff is worried about the potential treatment of Jordan's large central bank claims on Iraq (which they distinguish from other countries' credits to Iraq), as well as by what they see as elevated military spending. End Summary.

¶2. (C) IMF Mission Leader for Jordan Ihsan Mansur and mission members briefed the DCM, the USAID Mission Director and other embassy staff on November 4 on their findings toward the mid-point of an on-going visit to Amman. The mission estimated that Jordan would meet or exceed growth and deficit reduction objectives for 2003. Growth would range between 3 and 4% and the deficit would reach 2.5% of GDP or below -- thanks to the cash assistance already provided by the United States, which had offset war-related budget shortfalls.

Budget Crunch in 2004

¶3. (C) The IMF team felt that Jordan had "no economic need" for additional cash assistance during 2003. Cash assistance -- including the recently appropriately $100 million in supplemental aid and the "regular" FY04 cash transfer -- would be more useful in 2004, when Jordan could face a budget and balance of payments "crunch" from lower grant aid and higher oil import costs. (The mission said it was estimating that Jordan would pay market prices for oil imports from the second half of 2004.)

New Government's Fiscal Commitment "Untested"

¶4. (C) Expressing a concern about the new government's commitment to fiscal discipline nearly identical to that in ref A, the IMF mission suggested that it would be useful for the U.S. to find ways to reinforce the new finance minister's efforts to keep deficit reduction on track, including by conditioning delivery of U.S. cash transfers on maintenance of sound budget policies. In particular, the team mentioned that it could be useful to use new cash transfers to reinforce commitments made to the U.S. and IMF over the past year to increase the base and rate of the value-added tax and to reduce subsidies on oil products. They also asked that the U.S. convey the message that it was in the Jordanians best interest to continue to work closely with the Fund, even after the July expiration of the current program. (They noted that non-binding "enhanced staff monitoring" would continue through 2005.)

SETP Funds Should be "Well-Spent"

¶5. (C) The Fund staff said that it did not have a preference on whether U.S. aid was used to fund Social and Economic Transformation Plan (SETP) projects or regular budget needs. In their view, the bottom line was the same. Their main concern about the SETP was the "quality of spending." Although the IMF did not look at the detailed breakdown of SETP spending, it was concerned that appropriate financial controls should be in place , which they do not appear to be. (See ref B for former Finance Minister Marto's similar concerns about the SETP.)

Iraqi "Debt" Something Else

¶6. (C) Asked about the Central Bank of Jordan's $1.5 billion in claims on the Central Bank of Iraq, the staff members said that in their opinion this did not constitute "debt" in the way the Paris Club looks at debt. Rather, they said it should be viewed as "cash payments" that were due and not paid. Furthermore, while not considered free reserves, these claims are treated as assets in the Bank's balance sheet. Should inclusion of these claims in a multilateral restructuring of Iraq's debt require the Central Bank to write-off such a large amount, the Bank could become insolvent. This would mean that the Government of Jordan would be legally required to recapitalize the Bank -- creating an equivalent demand on the central government's budget. "Don't destroy one country to save another," they advised.

Military Spending Needs to be "Rationalized"

¶7. (C) As for longer-term issues, team members said they would be turning their attention to Jordan's level of military spending which they said was among the highest in the world per capita or as a share of GDP. Ironically, they noted, U.S. military aid in the form of equipment only aggravated the demands on the budget for personnel and recurring costs. Obviously, this was a very difficult problem, but the team felt there was no alternative to taking a close look at rationalizing the level of military expenditure.

Comment

¶8. (C) As the IMF staff points out, Jordan continues to face financial challenges. We think the advice to transfer U.S. cash aid in Jordan's 2004 budget year (beginning January 1) and to condition it on budgetary and policy performance is well-placed. Dr. Abu Hammour, the new and politically untested finance minister, and other ministers of like mind will no doubt welcome the additional leverage this will given him in keeping the 2004 deficit under control.
GNEHM